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No. 02-938

IN THE
Supreme Court of the United States

JOHN K. CASTLE, ET AL.,

Petitioners,

v.

UNITED STATES,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Federal Circuit

REPLY BRIEF FOR PETITIONERS

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REPLY BRIEF FOR PETITIONERS

By denying restitution to petitioners despite their performance of the terms of their contract with the government, and by adhering to a concededly "more stringent" test for third-party-beneficiary standing than that set forth by the RESTATEMENT and adopted by the Ninth Circuit, the court of appeals in this case unquestionably adopted unique rules of law to benefit the government in contract cases. In so doing, the court created or exacerbated two circuit conflicts and violated the clear mandate of this Court's decision in *Mobil Oil Exploration & Producing Southeast, Inc. v. United States*, 530 U.S. 604, 607 (2000), which instructs the Federal Circuit to follow the RESTATEMENT in government contract cases. The government's protestations to the contrary are unpersuasive, and plenary review is warranted.

I. The Federal Circuit's Denial Of Restitution Warrants Review

1. The government attempts to defend the decision below by misstating well-established principles of restitution contained in the RESTATEMENT (SECOND) OF CONTRACTS and the RESTATEMENT OF RESTITUTION. Like the court below, the government asserts that a nonbreaching party who performs under a contract is not entitled to restitution unless the party was *obligated* to perform. Opp. 9-10 ("Because Castle and Harlan were not contractually obliged to invest in New Western Empire, the court of appeals correctly held that they were not entitled to recover the $502,000 investment they in fact made."); *see also id.* at 13. Thus, the government endorses the Federal Circuit's express holding that restitution of a benefit conferred through contract performance

is precluded unless there was a prior contractual duty to perform. *See* Pet. App. 21a (denying restitution despite petitioners' performance because, according to the court, the capital provided by petitioners was "contributed voluntarily, beyond their contractual obligations"). It is that acknowledged holding that conflicts with settled principles of contract law and that amounts to a special rule now applicable only in government contract cases, in flagrant violation of the dictates of *Mobil Oil*.

The government does not dispute that the decision below effectively precludes restitution in *any* unilateral contract case, because it holds that restitution is unavailable to one who performs under a contract with no preexisting obligation to do so—the very definition of a unilateral contract. *See* Pet. 11-12.[1] Yet, the law is

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[1] The government seeks to confuse the issues by asserting that "[t]he court of appeals viewed the case as involving a bilateral contract because that is the way petitioners presented it." Opp. 10. The government badly misreads the decision below. While petitioners argued below that the contract was bilateral in nature, the court of appeals squarely rejected that assertion, concluding that petitioners did not "promise" to recapitalize Western Empire and thus were not obligated to do so. Pet. App. 20a-21a. Since the court of appeals left undisturbed the trial court's determination that a contract was formed, the purported absence of a promise binding petitioners necessarily means that the court of appeals viewed the contract as unilateral in nature. *See, e.g.*, BLACK'S LAW DICT. 326 (7th ed. 1999) (defining "Unilateral Contract" as "[a] contract in which only one party makes a promise" and thus "'only one party is ever under an obligation'") (quoting John D. Calamari & Joseph M. Perillo, THE LAW OF CONTRACTS § 2-10(a), at 64-65 (4th ed. 1998)). In any event, it makes no difference whether the contract is characterized as unilateral or bilateral. The key point, which the government strives mightily to obfuscate, is that petitioners un-

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clear that restitution is an available remedy for breach of a unilateral contract in which the non-breaching party performs and confers a benefit on the other party. *See* RESTATEMENT (SECOND) OF CONTRACTS § 373 (1981).

The Federal Circuit's holding (and the government's mischaracterization of the law of restitution) runs directly contrary to the well-established principles of restitution embodied in the RESTATEMENTS. As demonstrated in the petition, the RESTATEMENTS provide that, when a non-breaching party confers a benefit on the other party through performance under the contract, restitution must be paid *regardless* of whether the non-breaching party had a preexisting *obligation* to confer that benefit.[2] The Federal Circuit's failure to apply this rule to require restitution of petitioners' infusion of capital under the contract thus conflicts with this Court's instruction in *Mobil Oil* to adhere to the RESTATEMENT in government contract cases. *See* 530 U.S. at 607.

2. The government erroneously contends that Castle and Harlan did not in fact perform under the contract.

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questionably *performed* under the terms of the contract by contributing the $15.12 million in capital necessary to recapitalize the thrift (*see* Pet. App. 91a), and under the RESTATEMENTS and the law of contracts (except in the Federal Circuit) the government's failure to perform its side of the bargain entitles petitioners to restitution measured by the value of their performance.

2 *See, e.g.*, Pet. 12-13; RESTATEMENT § 373 (the non-breaching party to a contract "is entitled to restitution for any benefit that he has conferred on the other party by way of part performance or reliance"); *id.*, Chapter 16 (Remedies), Topic 4 (Restitution), Introductory Note, at 199; RESTATEMENT OF RESTITUTION § 108 (1937).

According to the government, "because any government 'offer' that occurred in this case did not by its plain terms require the infusion of capital by Castle and Harlan, any infusion of capital by them . . . ." Opp. 12; *see id.* at 13 ("The Restatement of Restitution makes clear that '[a] person who officiously confers a benefit upon another is not entitled to restitution therefor"). This assertion is false.

The trial court expressly found, without challenge from the court of appeals, that "what the government bargained for and received was an infusion of capital into an ailing bank and the subsequent operation of that bank in accordance with an approved business plan. The government got what it bargained for; hence, restitution is available." Pet. App. 91a-92a. The Federal Circuit did not dispute the trial court's finding that petitioners *in fact performed* under the contract by arranging for the capital infusion of $15.12 million into Western Empire. *Id.*

The record evidence, moreover, leaves no doubt that the trial court was correct in finding that petitioners performed under the contract. Pursuant to the contract's terms, Castle and Harlan agreed to organize an investor group "'in order to recapitalize the association'" and agreed that "'in no case will [the capital infusion] be less than the amount necessary to capitalize the existing assets at the required rate.'" Pet. App. 9a, 20a-21a (citations omitted). According to the government, the regulators did not seek an infusion of capital into the failing thrift, but instead found petitioners' capital contribution to constitute "officious" intermeddling. Opp. 13. That absurd proposition is refuted by the undisputed evidence that the government extensively negotiated the amount

of capital that would be infused. A5000140.[3] As this Court explained in *Winstar*, the very purpose of the *Winstar*-type contracts was to induce private investors to contribute capital and take over failing thrifts. *See United States v. Winstar Corp.*, 518 U.S. 839, 847-51 (1996); *id.* at 894; *id.* at 921 (Scalia, J., concurring).

Indeed, as the government's own documents in this case demonstrate, petitioners' contribution of capital was an express prerequisite to the government's approval of petitioners' proposed acquisition of Western Empire.[4] Thus, far from being "officious" conduct, petitioners' infusion of $15.12 million in capital into the failing thrift was an express government-imposed condition precedent to consummation of the proposed acquisition and was precisely what the government wanted in exchange for its contractual promises. Pet. App. 91a.

3. The government errs in attempting to distinguish the holdings in *Far West* and *RTC* on the ground that the investors in those cases were contractually obligated to perform. Opp. 13-14. The investors in those cases were no more obligated to contribute capital than the investors here. *See Far West v. OTS*, 119 F.3d 1358, 1364 (9th Cir. 1997); *RTC v. FSLIC*, 25 F.3d 1493, 1505

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[3] Indeed, the government brought a counterclaim against petitioners, alleging that they had "breached their obligations under the [contract] by failing to infuse sufficient capital into WESL." A5001809.

[4] *See* PX 78, at 9 (regulators required "the level and quality of the applicant's capital [to be] sufficient" in order to approve the acquisition and deemed this criterion satisfied because the "applicants propose to infuse capital . . .").

(10th Cir. 1994). The government's assertion that Castle and Harlan had "*disclaimed* any obligation" to contribute capital is simply false. Opp. 14. As the very document cited by the government reveals, Castle and Harlan disclaimed only the obligation to *maintain* the capital level *after* the initial recapitalization to the required level; they clearly were required to provide for the *initial* recapitalization in order to qualify for the benefits promised by the government. Pet. App. 21a. Thus, in all material respects, the investors were identically situated. The Federal Circuit's approach denying restitution simply cannot be reconciled with *Far West* and *RTC*. *See* Pet. 15-17.[5]

Finally, the government argues that any conflict between the decision below and the holdings of the Ninth and Tenth Circuits in *Far West* and *RTC* does not warrant this Court's review because all of the *Winstar*-related cases currently pending are located in the Court of Federal Claims or the Federal Circuit. Opp. 15. To the contrary, this conflict confirms that the Federal Circuit has adopted a special rule applicable only in gov-

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[5] In addition, as explained above, restitution is required for "any benefit that [the non-breaching party] has conferred on the other party by way of part performance or reliance." RESTATEMENT § 373. Thus, whether the non-breaching party was contractually bound to perform is of no significance if the party did in fact perform under the contract and conferred a benefit on the other party. *See id.* The government has, therefore, presented a distinction with no legal relevance to the issue whether restitution is required. There is no dispute that the investors in this case and in *Far West* and *RTC* performed under their contracts by contributing capital. Yet the Federal Circuit, unlike the Ninth and Tenth Circuits, denied petitioners restitution, creating a square circuit conflict.

ernment contract cases. The Ninth Circuit followed the RESTATEMENT. The court below rejected the Ninth Circuit's approach. This alone establishes a violation of *Mobil Oil*. In addition, even where the Federal Circuit's jurisdiction is "[i]n certain respects . . . exclusive," "[t]he issues arising in this type of litigation, involving many of the legal obligations of the United States, can have a special importance that warrants review by the Supreme Court." ROBERT L. STERN, ET AL., SUPREME COURT PRACTICE § 4.21, at 264 (8th ed. 2002) (citing, *inter alia*, *Winstar*, 518 U.S. at 839).

II. The Federal Circuit's Denial Of Standing Warrants Review

As the Federal Circuit expressly acknowledged, the decision below applied a special, "more stringent" rule to determine third-party beneficiary status in cases involving government contracts, a rule that conflicts with the RESTATEMENT (and thus with *Mobil Oil*), and with the Ninth Circuit's decision in *Far West*. Pet. App. 16a. Under the RESTATEMENT, a third party who is an "intended beneficiary" of a contract has standing to sue for its breach. *See* RESTATEMENT §§ 302, 304. Applying this test, the trial court found that "[i]t is clear . . . that the 'implied intention' of the parties was to benefit the investors" (Pet. App. 122a-123a)—a finding that the court below did not overturn.

The government contends that the Federal Circuit reviewed *de novo* and "squarely rejected" the trial court's finding that the non-signatory petitioners were intended beneficiaries under the *Far West* standard. Opp. 19. To the contrary, the court below left that finding undisturbed, but held instead that, under the admittedly "more stringent" test of *Glass*, the non-signatory petitioners

were not intended beneficiaries. *See* Pet. App. 16a-18a.

Thus, the Federal Circuit's holding is directly inconsistent with *Far* West, which applied the RESTATEMENT'S test and found similarly situated investors to be intended beneficiaries. *See* 119 F.3d at 1363-64.[6] Indeed, the Federal Circuit expressly rejected the approach used in *Far West*. Pet. App. 16a. Under its "more stringent" test for third-party beneficiary status, the Federal Circuit required not just an intent to benefit the third party, but an intent to benefit the third party *directly*. *Id.* at 16a-17a.[7] As the court below made clear (*id.*), the

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6 The government erroneously attempts to distinguish *Far West* on the purported ground that "[n]o . . . identification of the investor petitioners as intended third-party beneficiaries exists in this case." Opp. 21. Contrary to the government's claim, the regulators *required* that the non-signatory petitioners here be identified to the government, by name and amount of contribution, prior to the closing. In addition, the government erroneously asserts that the non-signatory petitioners were not induced to invest by the government's promises. Opp. 19 n.9 ("The private placement memorandum made no reference to any contract with the regulators"). In fact, before making any infusion of capital, the investors each received a Supplement to Offering Memorandum, dated December 20, 1988, which described the key terms of the contract with the regulators, including the fact that the "regulatory capital requirements [would be] substantially less stringent than under current FSLIC regulations." DX 37, at CH-000944. At the regulators' request, the government received copies of all such documents.

7 The cases relied on by the government in support of the "direct benefit" test (Opp. 16-17) are inapposite; the direct benefit test is inapplicable to contracts, such as here, that are intended to benefit identifiable individuals rather than members of the public at large. *See* RESTATEMENT § 313 & cmt. *a*. In addition, the government's assertion that the non-signatory petitioners were "inci-

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difference in the tests was outcome determinative. Thus, by failing to apply the RESTATEMENT test, the decision below conflicts with both *Mobil Oil* and *Far West.*

III. The Federal Circuit's Denial Of Just Compensation Merits Review

The government fails to refute petitioners' showing that the court of appeals erred in concluding that a party to a government contract loses its constitutional right to just compensation in the event of a subsequent taking.

First, the court improperly segmented petitioners' property into two parts: their contractual rights and their ownership of Western Empire. *But see Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 327 (2002) (property must be defined based on "'the parcel as a whole'"); *Monongahela Navigation Co. v. United States*, 148 U.S. 312, 328-30 (1893) (just compensation required for *entire value* of business, including physical assets and government contracts).[8]

Second, the Federal Circuit's holding that petitioners suffered no taking because they "retained the full range of [contract] remedies" (*see* Pet. App. 26a) conflicts with, among other cases, *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1011 (1984), and *Kaiser Aetna v. United*

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dental beneficiaries" not entitled to standing (*see* Opp. 20) finds no support in the RESTATEMENT. *See* RESTATEMENT § 302, illus. 2.

8 The government's attempt to distinguish *Monongahela* (Opp. 24) is unavailing; the fact that the contractual right at issue there was granted by one sovereign and taken by another does not affect the Court's holding defining the relevant property interest.

States, 444 U.S. 164, 179-80 (1979).[9] *See* Pet. 27-29. The government's assertion that "neither case involved a contract" (Opp. 25) is wholly unpersuasive; to suggest that parties to a non-contractual, statutory promise (*Monsanto*) and an implicit promise (*Kaiser*) are entitled to a greater degree of constitutional protection than those like petitioners who receive a written promise from the government is nothing short of absurd.

CONCLUSION

The petition for a writ of certiorari should be granted.[10]

Respectfully submitted.

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[9] The government's claim that contract remedies are exclusive also conflicts with the *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 155 (1974) (government must make up any "constitutional shortfall" between just compensation and the remedy provided). Here, the amount of just compensation exceeds the trial court's award of restitution because, among other reasons, the Constitution requires the payment of prejudgment interest. *See, e.g., Library of Congress v. Shaw*, 478 U.S. 310, 317 n.5 (1986).

[10] As noted in the petition (Pet. 7 n.1), the Federal Circuit improperly refused to file petitioners' petition for rehearing *en banc* in this case. After petitioners filed a petition for mandamus with this Court challenging that erroneous decision, the Clerk of the Federal Circuit suggested that the parties file a joint motion asking the Federal Circuit to reconsider its erroneous refusal to file the petition for rehearing. The parties did so, and the Federal Circuit granted the motion. The court then denied rehearing *en banc* on May 1, 2003. Accordingly, the petition for certioriari is now ripe for this Court's consideration.

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